

Joint Economic Committee WEEKLY ECONOMIC DIGEST

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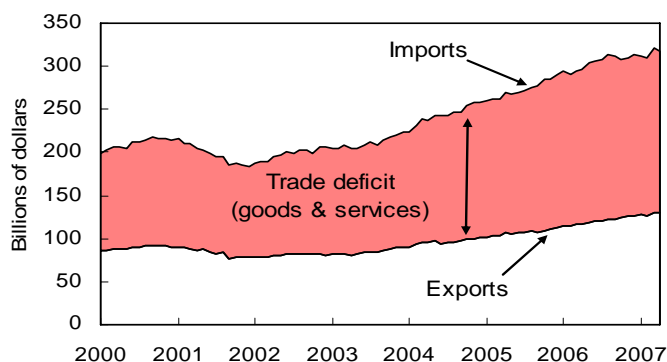
June 11, 2007

ECONOMIC NEWS

A Week of Surprises

The trade deficit declined unexpectedly in April but remains large. Exports of goods and services increased by a scant \$0.2 billion last month, but imports declined by \$3.6 billion. As a result, the deficit for international trade in goods and services declined by \$3.9 billion to \$58.5 billion. The April trade gap was substantially lower than the level that market analysts had anticipated. Even so, the trade deficit remains unsustainably large (see chart) and exports will have to grow substantially more rapidly than imports over a prolonged period for the trade balance to improve significantly.

U.S. International Trade in Goods and Services



Source: Census Bureau and Bureau of Economic Analysis, U.S. Department of Commerce.

Long-term interest rates rose sharply late last week. The interest rate on 10-year Treasury notes rose by 0.14 percentage point on Thursday to 5.11 percent—the largest daily gain in over three years—and has remained high in the days since then. The reasons for that sudden rise in the long-term rate are not fully clear. While such shifts sometimes stem from anticipations of higher inflation, financial market measures of inflationary expectations did not change much over the week.

First-quarter productivity growth was slower than previously believed. Output per hour worked in nonfarm businesses rose at a 1.0 percent annual rate in the first quarter, according to revised estimates by the Department of Labor. That was 0.7 percentage point below the Department's preliminary estimate of 1.7 percent. In contrast with the other economic news last week, the productivity revision was not a surprise as it largely reflected a downward revision to overall economic growth in the first quarter.

IN FOCUS

Marking Down the Outlook at Midyear

Reassessing the economic outlook is one of the important rites of summer for official forecasters. This summer, the forecast revisions are bound to reflect the slowing of economic growth and acceleration in energy prices already evidenced in the early part of the year. Last week, the Council of Economic Advisers issued a preview of its updated economic assumptions in which it expects that, over the course of 2007, economic growth will be slower and inflation higher than it had predicted six months ago. Forecast revisions by the Congressional Budget Office and the Federal Reserve to be released later in the summer are likely to go in the same general direction.

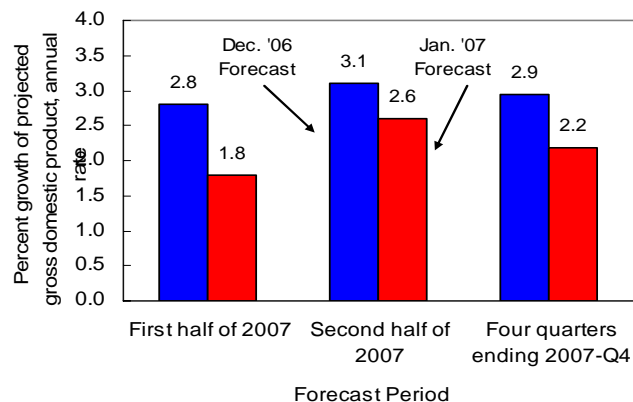
That trend is evident in the mid-year revisions by private-sector forecasters as well. Last week, the Livingston Survey—a semiannual survey of about 40 leading private-sector forecasters published by the Federal Reserve Bank of Philadelphia—dropped its growth forecast for real (inflation-adjusted) gross domestic product (GDP) to 2.2 percent over the course of this year. That is down 0.7 percentage point from the Survey's December prediction of 2.9 percent (see Snapshot).

In the first quarter, the economy grew at an unusually slow 0.6 percent annual rate. That was much slower than forecasters had predicted at the end of last year. Forecasters believe that growth has rebounded some since the first

Continued on reverse...

SNAPSHOT

Consensus of Forecasters Marks Down Its Outlook for Growth in 2007



Source: The Livingston Survey, Federal Reserve Bank of

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THE WEEK AHEAD

DAY	RELEASE
Tuesday 12	Monthly Treasury State of Receipts and Outlays of the U.S. Government (May 2007)
Wednesday 13	U.S. Import and Export Price Indexes (May 2007) Advance Monthly Sales for Retail and Food Services (May 2007) Manufacturing and Trade Inventories and Sales (April 2007)
Thursday 14	Joint Economic Hearing: "Importing Success: Why Work-Family Policies from Abroad Make Economic Sense for the U.S." 216 Hart Senate Office Building at 10 AM Producer Price Indexes (May 2007)
Friday 15	U.S. International Transactions (First quarter 2007) Consumer Price Index (May 2007) Industrial Production and Capacity Utilization (May 2007)

**FRIDAY,
June 15th:**
**U.S. current
account
balance for
first quarter**

THE ECONOMY AT A GLANCE

KEY INDICATORS	MONTH			QUARTER			YEAR	
	May	Apr	Mar	2007 Q1	2006 Q4	2006 Q3	2006	2005
Real GDP Growth (%)	—	—	—	0.6	2.5	2.0	3.3	3.2
Unemployment (% of labor force)	4.5	4.5	4.4	4.5	4.5	4.7	4.6	5.1
Labor Productivity Growth (%)	—	—	—	1.0	2.1	-0.5	1.6	2.1
Labor Compensation Growth (%)	—	—	—	3.2	3.6	3.6	3.1	3.3
CPI-U Inflation (%)	n.a.	4.9	7.4	3.8	-2.1	3.1	3.2	3.4
Core CPI-U Inflation (%)	n.a.	2.4	1.2	2.3	1.9	3.0	2.5	2.2

Sources: Bureau of Economic Analysis, U.S. Department of Commerce; Bureau of Labor Statistics, Department of Labor.

Notes: Except where otherwise noted, values in the table represent percent changes at seasonally adjusted annual rates. Productivity is output per hour worked in private nonfarm businesses. The Employment Cost Index is for civilian workers in government and business. Core CPI-U inflation is the percent change in the CPI-U excluding food and energy as reported by the Bureau of Labor Statistics. The designation "n.a." denotes that data are not yet available.

IN FOCUS (Continued)

quarter and the narrowing in the April trade gap is an early indication that the some of the drag on first-quarter growth may be dissipating. The updated Livingston consensus also expects new homebuilding to end the year little changed from the average over the first quarter. In other words, while declines in homebuilding are expected to end, a strong rebound is not expected anytime soon.

All in all, the consensus expects the pace of growth in the second half of the year to be just 2.6 percent (annual rate). That would be below the range of growth rates most economists believe to be sustainable over the medium term.

The Livingston Survey also shows that forecasters have raised their inflation predictions for 2007 over the past six months. Since the start of the year, inflation in the consumer price index (CPI) has risen by 4.8 percent at annual rate. That's well above the 2.5 percent rise in 2006. Energy prices have risen at an average annual pace of 25.3 percent since the end of last year, contributing 2 full percentage points to the rise in the overall CPI. While the Livingston Survey forecasters expect some moderation of the CPI in the second half of year, the acceleration already evident has contributed to the upward revision in their inflation forecast for 2007. The Survey now expects CPI inflation to average 3.1 percent over the course of 2007, as compared with the forecast of 2.6 percent it made in December.

Certainly, the economic outlook might well change further between now and the end of the year. But the general direction of mid-year revisions to the basic economic outlook is already set.